

**DEPARTMENT OF STATE REVENUE  
LETTER OF FINDINGS NUMBER: 98-0270 RST**

**Sales/Use Tax — Case Palletizers  
Tax Administration — Penalty  
For Tax Periods: 1994 through 1996**

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**ISSUES**

**I. Sales/Use Tax — Case Palletizers**

**Authority:** IC 6-2.5-5-3; 45 IAC 2.2-5-8(d)  
*Indiana Department of State Revenue v. Cave Stone, Inc.*, 457 N.E.2d 520 (Ind. 1983).

Taxpayer protests the proposed assessment of Indiana use tax on its purchase of case palletizers.

**II. Tax Administration — Penalty**

**Authority:** IC 6-8.1-10-2; IC 6-8-10-2.1;  
45 IAC 15-11-2; 45 IAC 2.2-3-20

Taxpayer protests the imposition of a ten-percent (10%) negligence penalty.

**STATEMENT OF FACTS**

Taxpayer is engaged in the business of processing and marketing a variety of food products. During the 1994 tax year, taxpayer purchased three (3) automated case palletizers. At the time of sale, Indiana sales tax was not paid on these purchases. Consequently, an assessment of use tax was proposed by Audit. Taxpayer now protests these assessments.

## **I. Sales/Use Tax — Case Palletizers**

### **DISCUSSION**

Taxpayer purchased three (3) automated case palletizers in 1994. The palletizers were used, according to taxpayer, during the preparation of food products. (Taxpayer is engaged in the business of food processing.) Given such use, taxpayer characterized the palletizers as “essential and integral” to its integrated production process. Taxpayer then reasons, pursuant to IC 6-2.5-5-3, that its automated palletizers should be exempt from Indiana sales and use taxes. Audit, however, has disagreed with taxpayer’s conclusions and assessed use tax on these purchases.

#### **Rule**

In Indiana, an excise tax (sales tax) is imposed on retail transactions. A complementary excise tax (use tax) is imposed on tangible personal property that is stored, used, or consumed in this state. Several exemptions from these taxes are available. Taxpayer relies on one of the industrial exemptions.

Referred to as the equipment exemption, IC 6-2.5-5-3(b) instructs:

Transactions involving manufacturing machinery, tools and equipment are exempt from the state gross retail tax [sales tax] if the person acquiring that property acquires it for *direct use in the direct production*, manufacture, fabrication, assembly, extraction, processing, refining, or finishing of other tangible personal property. [Emphasis added.]

The equipment exemption upon which taxpayer relies contains the "double direct" language - language which describes a standard that can be met when a particular item is determined to be "essential and integral" to taxpayer's "integrated production process." *Indiana Department of State Revenue v. Cave Stone, Inc.*, 457 N.E.2d 520 (Ind. 1983).

#### **Department's Position**

Not surprisingly, no simple “bright line” test exists that would allow one to determine whether a piece of equipment qualifies for any of the industrial exemptions. As every taxpayer’s production process is unique, any determination necessarily requires, as a prerequisite, a fact-sensitive inquiry. In other words, resolution (i.e., whether the exemption applies or not) can be reached only after all facts have been gathered and evaluated.

At hearing, taxpayer provided the Department with credible evidence supporting its contention that the palletizers were, in fact, used in an essential step within its integrated production process. Consequently, the Department finds that taxpayer is entitled to employ the equipment exemption for its palletizers. *(A caveat: this is not an instance where taxpayer uses its automated palletizers in post-production shipping activities – activities in which all equipment used is taxable pursuant to IC 6-2.5-5-3 and 45 IAC 2.2-5-8(d)).*

### **FINDING**

Taxpayer's protest is sustained.

## **II. Tax Administration — Penalty**

### **DISCUSSION**

The taxpayer protests the imposition of the ten-percent (10%) negligence penalty.

The negligence penalty imposed under IC 6-8.1-10-2.1(e) may be waived by the Department where reasonable cause for the deficiency has been shown by the taxpayer. Specifically:

The department shall waive the negligence penalty imposed under IC 6-8.1-10-2.1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. 45 IAC 15-11-2(e).

The Department finds that since taxpayer has shown reasonable cause, the negligence penalty should be waived.

### **FINDING**

Taxpayer's protest is sustained.